

Somerville
Industries
Limited

Annual
Report
1974

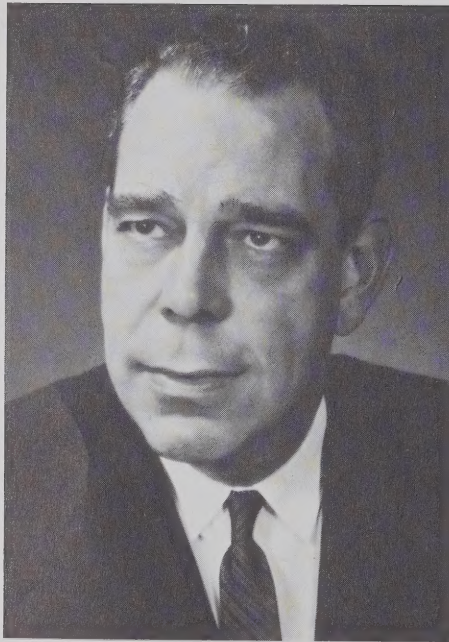
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Somerville

Somerville Industries, with its head office located in London, Ontario, operates eight plants—in Montreal, Toronto, Bramalea, Windsor, Winnipeg and London. The Company produces folding cartons, flexible packaging, games and puzzles, vacuum formed, compression and injection moulded plastic, automotive products, and provides merchandising services.

Report to Shareholders



The Company's financial results for 1974 represented an all-time record in both sales volume and net income.

Consolidated net sales for year were \$61,647,000 — an improvement of \$10,390,000, or 20% over the year previous. Packaging sales reached \$44,991,000 and were \$8,535,000 or 23% higher than in 1973. The sale of automotive products dropped by \$618,000 (9%) below 1973 volume. Other segments of the company showed a sales improvement of \$2,473,000, to a level of \$10,472,000, mainly due to a strong performance in the Plastics and Games Division.

The selling climate was excellent for most Divisions of the Company for the greater part of the year, in the face of raw material shortages and consequently uncertain deliveries prevalent in the first half of 1974. Order backlogs were heavy, probably reflecting a degree of over-buying in most of the major markets served by the Company. This resulted in a softening of market demand in the last quarter of 1974 and the slow-down is expected to continue until existing client inventories are depleted.

The Automotive Division suffered from the developing crisis in the major industry it serves. A narrowing of this specialized market was forecast very early in 1974 but the eventual cut-back in North American automobile production was far more severe than

anticipated. Higher sales of non-automotive compression moulded plastic products offset at least some of the unexpected decline in demand for automotive components.

Net income for 1974, at \$2,795,000, exceeded 1973 earnings by \$1,060,000 — an increase of 61%. It should be noted in the interest of proper comparison, that the income improvement over 1973 was considerably enhanced by a diminished profit performance in the earlier year, during which constantly inflating costs were not recovered. Net income for 1974 was at the rate of 4.5% to sales, by comparison with a ratio of 3.4% in 1973.

The pressures of high product demand, coupled with serious raw material shortages, inevitably caused extra operating costs, because of juggled production schedules, premium time labour, and heavy raw material inventories, which had to be carried in order to ensure continuity of supply to our clients. The need to bring in basic materials when available, rather than doing so as required for production, created unusually high interest expenses on short term borrowings.

In general, the Company's satisfactory profit performance resulted from excellent cost control at the operating level.

Fixed asset purchases totalled \$896,000 in 1974. The bulk of this expenditure was made to update Packaging and Plastics equipment. An accelerated program to improve and expand productive capacity in all divisions will continue through 1975 and 1976.

A substantial improvement of working capital was recorded in 1974, primarily as a result of improved profitability and reduced capital expenditures; the latter was held to a lower than expected total in order to conserve operating cash. At the year-end working capital was \$15,168,000 as compared with \$13,742,000 at the end of 1973.

Two major appointments were made at the corporate executive level immediately following the 1974 year-end. L. A. Biddie, formerly General Manager of the Ontario Packaging Divisions, has been appointed Group Vice-President with responsibility for all packaging operations. G. J. Deignan has been appointed Director of Corporate Planning for the Packaging Divisions, Mr. Deignan was formerly General Manager of the Montreal Packaging Division. Both of these experienced and capable executives will add depth and strength to the corporate management group.

Finally, it is entirely appropriate to congratulate and thank all members of the Somerville staff in the various divisions of the Company for their individual contributions to a successful year. The high levels of activity prevailing in most divisions for the greater part of 1974 imposed a heavy demand on the talents and energies of the operating staff and their response — which was both positive and effective — is sincerely appreciated. The co-operation and hard work of all the people who make up the organization made it possible for the Company to maintain its reputation for quality and service to its clients, in the face of many difficulties.

Present indications are that there will be no abatement of problems and pressure in 1975. The overriding problem of continuing inflation may be expected to continue. Raw materials are now in freer supply and this fact has fostered a return to more normal buying patterns — although a return to restricted supply conditions, either toward the end of 1975 or in the early part of 1976, is being freely predicted — notably in the pulp and paper industry.

The Company is well prepared to meet more highly competitive conditions, through new product development, aggressive selling, and tighter internal cost controls and, in this, the continuing support of all employees will be a vital factor.

John G. Church,
Chairman and President.

Consolidated Balance Sheet

Somerville Industries Limited
(incorporated under the laws of Canada)
As at December 31, 1974
(in thousands of dollars)

Assets	1974	1973
Current assets		
Cash	\$ 7	\$ 7
Accounts receivable (note 2)	7,432	7,040
Inventories (note 1)	15,598	11,629
Prepaid expenses	172	386
	23,209	19,062
Investments		
Shares in 50% owned company—Mastico Industries Limited—at equity value	431	410
Sinking fund re preferred shares—government and industrial bonds at market values (cost—\$112,092)	101	100
	532	510
Unamortized debt financing costs (note 1)	245	259
Fixed assets (note 1)		
Land, buildings and equipment	24,376	23,655
Less accumulated depreciation	14,201	13,347
	10,175	10,308
	\$34,161	\$30,139

Approved by the Board
J. G. Church, Director
I. A. MacDonald, Director

Liabilities	1974	1973
Current liabilities		
Bank advances	\$ 3,567	\$ 1,639
Accounts payable and accrued liabilities (note 2)	3,099	3,472
Taxes payable	1,253	186
Dividends payable	22	23
Long-term debt payable within one year	100	
	8,041	5,320
Long-term debt (note 3)	8,476	8,576
Deferred income taxes	2,447	2,243
Shareholders' equity		
Capital stock (note 4)	1,934	1,985
Retained earnings (note 5)	12,341	11,093
Excess of appraised value of fixed assets over cost (note 1)	922	922
	15,197	14,000
	\$34,161	\$30,139

Consolidated Statement of Retained Earnings

Somerville Industries Limited
Year ended December 31, 1974
(in thousands of dollars)

	1974	1973
Retained earnings at beginning of year	\$11,093	\$10,612
Add net income for the year	2,795	1,735
	13,888	12,347
Deduct dividends		
Preferred shares	89	94
Common shares	1,458	1,160
	1,547	1,254
Retained earnings at end of year	\$12,341	\$11,093

Consolidated Statement of Income

Somerville Industries Limited
Year ended December 31, 1974
(in thousands of dollars)

	1974	1973
Net sales	\$61,647	\$51,257
Costs, excluding expenses shown below	55,097	46,806
Operating income, before undernoted items	6,550	4,451
Deduct		
Depreciation	1,029	1,092
Interest on long-term debt	712	556
Amortization of debt financing costs	14	14
Other interest	288	96
	2,043	1,758
Operating income	4,507	2,693
Equity in net income of Mastico Industries Limited	261	170
Income before income taxes	4,768	2,863
Income taxes	1,973	1,128
Net income for the year	\$ 2,795	\$ 1,735
Earnings per common share	\$ 7.59	\$ 4.60

Consolidated Statement of Changes in Financial Position

Somerville Industries Limited
Year ended December 31, 1974
(in thousands of dollars)

	1974	1973
Working capital derived from		
Operations		
Net income for the year	\$ 2,795	\$ 1,735
Items not involving working capital		
Depreciation	1,029	1,092
Deferred income taxes	204	141
Net increase in equity in Mastico Industries Limited	(21)	(20)
Amortization of debt financing costs	14	14
	4,021	2,962
Proceeds from Series A debenture issue		8,000
	4,021	10,962
Working capital applied to		
Purchase of fixed assets (net of disposals)	896	1,240
Purchase of preferred shares for cancellation	51	96
Dividends to shareholders	1,547	1,254
Reduction in long-term debt	100	107
Debt financing costs related to debenture issue		273
Sundry items (net)	1	(2)
	2,595	2,968
Increase in working capital	1,426	7,994
Working capital at beginning of year	13,742	5,748
Working capital at end of year	\$15,168	\$13,742

Notes to Consolidated Financial Statements

Somerville Industries Limited
December 31, 1974

1. Accounting policies

Principles of consolidation

The consolidated financial statements include the accounts of Canadian Folding Cartons Limited and Somerville Automotive Trim Limited. The business formerly conducted by these wholly-owned inactive subsidiaries is now being carried on by the Canadian Folding Cartons Division and the Somerville Automotive Trim Division of the Company.

Inventories

Inventories are valued at the lower of cost and net realizable value.

	1974	1973
Raw materials, goods in process and supplies	\$ 9,336,880	\$ 7,483,886
Finished goods	6,261,135	4,144,797
	<u>\$15,598,015</u>	<u>\$11,628,683</u>

Unamortized debt financing costs

Debt financing costs related to the 8½ % Series A sinking fund debentures are being amortized over the twenty year term of the issue on a straight-line basis.

Fixed assets and depreciation

Buildings and equipment are stated at cost except for buildings owned in 1951 and equipment owned in 1955 which are stated at depreciated replacement values in accordance with appraisals made in those years. Other fixed assets and additions subsequent to the appraisals have been shown at cost.

	1974	1973
Land and buildings	\$ 6,159,777	\$ 6,093,971
Machinery and equipment	18,216,107	17,561,346
	<u>\$24,375,884</u>	<u>\$23,655,317</u>

Depreciation is provided on a straight-line basis over the estimated useful lives of fixed assets.

2. Accounts receivable and accounts payable

Included in accounts receivable is an amount of \$481,843 owing from, and in accounts payable an amount of \$57,801 owing to affiliated companies. In 1973, the amounts were \$447,354 and \$121,892 respectively.

3. Long-term debt

	1974	1973
Debentures outstanding		
8½ % sinking fund debentures		
Series A due April 1, 1993	\$7,900,000	\$7,900,000
First mortgage bonds outstanding		
6% sinking fund bonds		
Series B due June 15, 1977	676,000	676,000
	<u>8,576,000</u>	<u>8,576,000</u>
Less payable within one year	100,000	
Total long-term debt	<u>\$8,476,000</u>	<u>\$8,576,000</u>

The first mortgage bonds are secured by a first floating charge on the assets of the Company.

Under the terms of the Trust Indenture the 8½ % sinking fund debentures, Series A, are secured by a floating charge on the assets of the Company subject to a prior charge securing the first mortgage bonds.

Aggregate sinking fund requirements during the next five fiscal years are as follows: 1975—\$100,000; 1976—\$176,000; 1977—\$700,000; 1978—\$100,000; 1979—\$180,000.

4. Capital stock

	Number of shares		Amount	
	1974	1973	1974	1973
Preferred cumulative, redeemable shares, par value \$50 each, issuable in series				
Authorized	100,000	100,000		
Less purchased for cancellation	8,436	7,431		
	<u>91,564</u>	<u>92,569</u>		
Issued and outstanding—\$2.80 sinking fund cumulative preferred shares, 1953 series redeemable at \$51 per share	31,564	32,569	\$1,578,200	\$1,628,450
Common shares without par value				
Authorized	500,000	500,000		
Issued and outstanding	356,300	356,300	356,300	356,300
			<u>\$1,934,500</u>	<u>\$1,984,750</u>

5. Retained earnings

Retained earnings include an amount of \$50,250 set aside as capital surplus in connection with the redemption of preferred shares as required by Section 62 of the Canada Corporations Act.

6. Long-term leases

Long-term leases entered into by the Company extend into the year 1988. Under the terms of such leases, the aggregate rental amounts to \$1,713,929. The maximum annual rent payable thereunder for the years 1975 to 1979 is \$153,803.

7. Statutory information

(a) Remuneration of directors and officers

	1974	1973
Number of directors	6	6
Aggregate remuneration as directors	Nil	Nil
Number of officers	4	3
Aggregate remuneration as officers	\$205,707	\$152,455
Number of officers who are directors	3	3

(b) Classes of business

In the opinion of the directors the classes of business contributing in excess of 10% of sales were as follows:

	Amount		Percentage	
	1974	1973	1974	1973
Packaging	\$44,991,046	\$36,456,387	72.9%	71.1%
Automotive products	6,184,076	6,802,231	10.1	13.3
Other	10,471,541	7,998,575	17.0	15.6
	<u>\$61,646,663</u>	<u>\$51,257,193</u>	<u>100.0%</u>	<u>100.0%</u>

Auditors' Report

To the Shareholders of
Somerville Industries Limited

We have examined the consolidated balance sheet of Somerville Industries Limited and its wholly owned subsidiaries as at December 31, 1974 and the consolidated statements of income, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion these consolidated financial statements present fairly the financial position of the companies as at December 31, 1974 and the results of their operations and the changes in their financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

The figures for 1973, included for comparative purposes, are based on the financial statements of that year which were reported upon by the companies' previous auditors.

A handwritten signature in cursive script, reading "Thomas Riddell & Co.", written in dark ink.

Chartered Accountants
London, Ontario
January 20, 1975

Directors

John G. Church
Ian A. MacDonald
Arie B. Van der Ende
W. Garfield Weston
W. Galen Weston
Thomas E. White

Officers

John G. Church
Chairman of the Board
and President
Ian A. MacDonald
Executive Vice-President
Arie B. Van der Ende
Secretary-Treasurer
Leslie A. Biddie
Group Vice-President —
Packaging Division
James C. Bacon
Group Vice-President —
Special Products Division

Head Office

Crumlin Side Road
London, Ontario

Transfer Agent

The Canada Trust Company
Toronto, London, Montreal,
Winnipeg and Vancouver

Stock Listing

Toronto Stock Exchange

Auditors

Thorne Riddell & Co.

